From: Gebhardt, Sharron
Sent: Monday, November 10, 2003 9:41 AM
To: Thrasher, Sandra Jo
Subject: FW: Oil valuation comments

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1-5.pdf (1 MB)

Please publish to the web- comments - AD04 Fed Oil Rule

-----Original Message-----
From: Lee E. Helfrich [mailto:helfrich@lnllaw.com]
Sent: Sunday, November 09, 2003 9:58 AM
To: Gebhardt, Sharron
Subject: Oil valuation comments

Dear Ms. Gebhardt: I have been trying to forward the comments and exhibits of California State Controller Steve Westly. Unfortunately, it appears that you are unable to receive the material as a whole. Therefore I will be sending it in five parts. This is part 1.

Attachment 1

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

INDEPENDENT PETROLEUM ASSOCIATION OF AMERICA,

Plaintiff,

v.

SYLVIA V. BACA, *et al.*,

Defendants.

AMERICAN PETROLEUM INSTITUTE,

Plaintiff,

v.

SYLVIA V. BACA, *et al.*,

Defendants.

Civ. No. 00-761 (RCL)

(consolidated for briefing with)

Civ. No. 00-887 (RCL)

STATUS REPORT

On April 24, 2002, Plaintiffs Independent Petroleum Association of America ("IPAA") and American Petroleum Institute ("API") notified the Court that they had petitioned for rehearing and rehearing en banc of the D.C. Circuit's decision in *Independent Petroleum Association of America v. Dewitt*, 279 F.3d 1036 (D.C. Cir. 2002), and that the D.C. Circuit had ordered that the government "file a response . . . to IPAA's observation that certain lease forms providing for the application of later-adopted regulations specify only those that relate to conservation."

Plaintiffs hereby notify the Court that on June 21, 2002, the D.C. Circuit denied their petitions for rehearing and rehearing en banc. Copies of the D.C. Circuit's Orders are attached for the Court's information. The time to file a petition for writ of certiorari of the D.C. Circuit's decision in *IPAA v. Dewitt* expires on September 19, 2002. SUP. CT. R.3.

July 25, 2002

Respectfully submitted,

Thomas J. Eastment / with permission LSM

THOMAS J. EASTMENT
BAKER & BOTTS, LLP
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L. Poe Leggette / with permission LSM

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NANCY L. PELL (No. 450443)
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(202) 662-0200

United States Court of Appeals

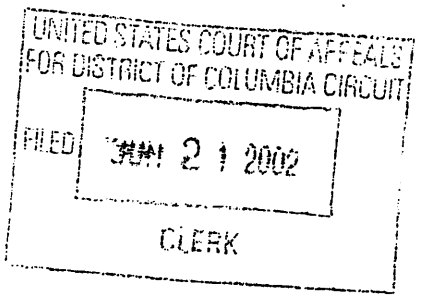
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 00-5404

September Term, 2001

98cv00531
98cv00631

Filed On:



Independent Petroleum Association of America,
Appellee

v.

Wallace P. DeWitt, Acting Assistance Secretary, for Land and Minerals Management, DOI and United States Department of the Interior,
Appellants

Consolidated with 00-5405

BEFORE: Ginsburg, Chief Judge, and Edwards, Sentelle, Henderson, Randolph,* Rogers, Tatel, and Garland,* Circuit Judges; Williams, Senior Circuit Judge

ORDER

Upon consideration of appellee Independent Petroleum Association of America's petition for rehearing en banc, the response thereto, and the absence of a request by any member of the court for a vote, it is

ORDERED that the petition be denied.

Per Curiam

FOR THE COURT:
Mark J. Langer, Clerk

BY: Michael C. McGrail
Deputy Clerk

* Circuit Judges Randolph and Garland did not participate in this matter.

United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 00-5404

September Term, 2001

98cv00531
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Filed On:

Independent Petroleum Association of America,
Appellee

v.

Wallace P. DeWitt, Acting Assistance Secretary, for Land and Minerals Management, DOI and United States Department of the Interior,
Appellants

Consolidated with 00-5405

BEFORE: Sentelle and Rogers, Circuit Judges, and Williams, Senior Circuit Judge

ORDER

Upon consideration of appellee American Petroleum Institute's petition for rehearing filed March 25, 2002, it is

ORDERED that the petition be denied.

Per Curiam

FOR THE COURT:
Mark J. Langer, Clerk

BY: Michael C. McGrail
Deputy Clerk

CERTIFICATE OF SERVICE

I, Laura S. Morton, certify that Plaintiffs' Status Report was served on the following individuals in the manner set forth below on the 25th day of July, 2002:

VIA FIRST CLASS MAIL

EDWARD S. GELDERMANN
U.S. Department of Justice
Environment and Natural Resources Division
P.O. Box 663
Washington, D.C. 20044-0663

GEOFFREY HEATH
Office of the Solicitor
U.S. Department of the Interior
1849 C Street, N.W.
Washington, D.C. 20240

Laura S. Morton

Attachment 1

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

INDEPENDENT PETROLEUM ASSOCIATION OF AMERICA, Plaintiff, v. SYLVIA V. BACA, *et al.*, Defendants.	Civ. No. 00-761 (RCL) (consolidated for briefing with)
AMERICAN PETROLEUM INSTITUTE, Plaintiff, v. SYLVIA V. BACA, *et al.*, Defendants.	Civ. No. 00-887 (RCL)

STATUS REPORT

On April 24, 2002, Plaintiffs Independent Petroleum Association of America ("IPAA") and American Petroleum Institute ("API") notified the Court that they had petitioned for rehearing and rehearing en banc of the D.C. Circuit's decision in *Independent Petroleum Association of America v. Dewitt*, 279 F.3d 1036 (D.C. Cir. 2002), and that the D.C. Circuit had ordered that the government "file a response . . . to IPAA's observation that certain lease forms providing for the application of later-adopted regulations specify only those that relate to conservation."

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July 25, 2002

Respectfully submitted,

Thomas J. Eastment / with permission LSM

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United States Court of Appeals

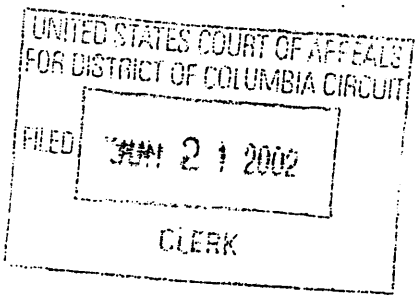
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 00-5404

September Term, 2001

98cv00531
98cv00631

Filed On:



Independent Petroleum Association of America,
Appellee

v.

Wallace P. DeWitt, Acting Assistance Secretary, for Land and Minerals Management, DOI and United States Department of the Interior,
Appellants

Consolidated with 00-5405

BEFORE: Ginsburg, Chief Judge, and Edwards, Sentelle, Henderson, Randolph,* Rogers, Tatel, and Garland,* Circuit Judges; Williams, Senior Circuit Judge

ORDER

Upon consideration of appellee Independent Petroleum Association of America's petition for rehearing en banc, the response thereto, and the absence of a request by any member of the court for a vote, it is

ORDERED that the petition be denied.

Per Curiam

FOR THE COURT:
Mark J. Langer, Clerk

BY: Michael C. McGrail
Deputy Clerk

* Circuit Judges Randolph and Garland did not participate in this matter.

United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 00-5404

September Term, 2001
98cv00531
98cv00631

Filed On:

Independent Petroleum Association of America,
Appellee

v.

Wallace P. DeWitt, Acting Assistance Secretary, for Land and Minerals Management, DOI and United States Department of the Interior,
Appellants

Consolidated with 00-5405

BEFORE: Sentelle and Rogers, Circuit Judges, and Williams, Senior Circuit Judge

ORDER

Upon consideration of appellee American Petroleum Institute's petition for rehearing filed March 25, 2002, it is

ORDERED that the petition be denied.

Per Curiam

FOR THE COURT:
Mark J. Langer, Clerk

BY: /s/ Michael C. McGrail
Michael C. McGrail
Deputy Clerk

CERTIFICATE OF SERVICE

I, Laura S. Morton, certify that Plaintiffs' Status Report was served on the following individuals in the manner set forth below on the 25th day of July, 2002:

VIA FIRST CLASS MAIL

EDWARD S. GELDERMANN
U.S. Department of Justice
Environment and Natural Resources Division
P.O. Box 663
Washington, D.C. 20044-0663

GEOFFREY HEATH
Office of the Solicitor
U.S. Department of the Interior
1849 C Street, N.W.
Washington, D.C. 20240

Laura S. Morton

Attachment 2
(excerpts)

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

INDEPENDENT PETROLEUM ASSOCIATION OF AMERICA, Plaintiff, v. SYLVIA V. BACA, *et al.*, Defendants.	Civ. No. 00-761 (RCL)
(consolidated for briefing with)	
AMERICAN PETROLEUM INSTITUTE, Plaintiff, v. SYLVIA V. BACA, *et al.*, Defendants.	Civ. No. 00-887 (RCL)

PLAINTIFF IPAA'S MOTION FOR SUMMARY JUDGMENT
AND MEMORANDUM IN SUPPORT

January 24, 2001

L. POE LEGGETTE (No. 430136)
NANCY L. PELL (No. 450443)
FULBRIGHT & JAWORSKI, LLP
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(202) 662-0200

25

TABLE OF CONTENTS

v. Seckinger, 397 U.S. 203, 210 (1970)). Furthermore, "no deference is due an agency's interpretation of contracts in which it has a proprietary interest." *Id.* (citing *Lockheed Martin IR Imaging Sys. Inc. v. West*, 108 F.3d 319, 322 (Fed. Cir. 1997); *Mesa Air Group Inc. v. Dep't of Transp.*, 87 F.3d 498, 506 (D.C. Cir. 1996)). Likewise, no deference is due an agency's interpretation of its own regulations that will affect a contract to which the agency is a party. *Id.* (citing *Transohio Sav. Bank v. Director, OTS*, 967 F.2d 598, 614 (D.C. Cir. 1992)).

C. THERE IS NO DUTY TO MARKET PRODUCTION AT NO COST TO THE FEDERAL LESSOR.

The new rule expressly requires the lessee to "market the oil for the mutual benefit of the lessee and the lessor at no cost to the Federal Government." (AR72M (30 C.F.R. § 206.106).) This Court struck down nearly identical duty to market language as arbitrary and capricious in *IPAA v. Armstrong*, 91 F. Supp. 2d at 130.[6/]

[6/] *Compare* 30 C.F.R. § 206.106 (2000) (oil rules) (AR72),

> You must place oil in marketable condition and market the oil for the mutual benefit of the lessee and the lessor at no cost to the Federal Government. If you use gross proceeds under an arm's-length contract in determining value, you must increase those gross proceeds to the extent that the purchaser, or any other person, provides certain services that the seller normally would be responsible to perform to place the oil in marketable condition or to market the oil,

with 30 C.F.R. §§ 206.152(i); 206.153(i) (1999) (gas rules),

> The lessee must place gas in marketable condition and market the gas for the mutual benefit of the lessee and the lessor at no cost to the Federal Government. Where the value established under this section is determined by a lessee's gross proceeds, that value will be increased to the extent that the gross proceeds have been reduced

(continued...)

During the rulemaking, industry expressed its concern that MMS would use the duty to market provision to second guess lessees' marketing decisions and to claim royalty on value added downstream of the lease in the midstream market. (AR2400-03; AR1734.) Activities such as storage, blending, risk management, aggregating volumes, and satisfying customer preferences add value to which the government is not entitled to share. (AR6198-204; AR2400-03.) Industry also argued that legally there is no express or implied duty to market at no cost. (*See, e.g.*, AR6198-204.) IPAA submitted a compendium of lease forms as evidence that the alleged duty to market could not be implied from the Department's leases. (AR2337.) Finally, industry submitted voluminous evidence that there are active markets at the lease and provided examples of royalty valuation procedures that could be used to value oil based on lease market values.[7/]

During the rulemaking, MMS explained at length its now-familiar arguments for an implied duty to market at no cost to the lessor. (AR9L-10M.) *See also IPAA v. Armstrong*, 91 F. Supp. 2d at 122-23 (this Court's summary of the Department's duty to market arguments). The agency also observed that the duty to market is the subject of pending litigation in *IPAA v. Armstrong* and the issue will likely be resolved by the courts. (AR37L.)

[6/](...continued)

> because the purchaser, or any other person, is providing certain services the cost of which ordinarily is the responsibility of the lessee to place the gas in marketable condition or to market the gas.

[7/] *See infra* note 13.

In *IPAA v. Armstrong*, this Court rejected the Department's position that it is entitled to royalty on the enhanced value of production sold downstream. 91 F. Supp. 2d at 125. The Court should reject the Department's identical assertion in this rulemaking.

1. The Duty to Market at No Cost to the Federal Lessor Is a Recent Concept.

In spite of the Department's assertion that it "has not knowingly permitted an allowance or deduction from royalty value for marketing costs," (AR9M), this is not the case. As this Court held, "Interior acknowledges, and the court finds as a matter of fact, that the downstream marketing costs made non-deductible by the [gas transportation] Rule, were, in fact, previously deducted by plaintiffs." *IPAA v. Armstrong*, 91 F. Supp. 2d at 123 (citation omitted). The Court further observed that "while reaping the benefits of a higher value downstream sale through a higher royalty, MMS did not simply free-ride on the lessees' efforts to obtain value for the gas." *Id.* at 120; *see also Marathon Oil Co. v. United States*, 604 F. Supp. 1375 (D. Alaska 1985), *aff'd*, 807 F.2d 759 (9th Cir. 1986.)[8/]

2. The Duty to Market Is Neither Express Nor Implied in Federal Lease Contracts.

Courts are not required to defer to an agency interpretation of a contract if the government is a party to the contract. *Lockheed Martin IR Imaging Sys. Inc. v. West*, 108 F.3d 319, 322 (Fed. Cir. 1997); *Mesa Air Group Inc. v. Dep't of Transp.*, 87 F.3d 498, 506 (D.C. Cir. 1996). And where

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8/ In 1990, subsequent to the decision in *Marathon*, the Department entered into a settlement agreement with the company. (*See* AR412-14; AR452-500.) Pursuant to the settlement, Marathon was to value Alaskan natural gas sold in Japan at Marathon's sales prices minus certain deductions. (*See* AR478-80.) The deductions included costs IBLA holds to be marketing costs. (*See* AR412-14 (citing *AnSon Co.*, 145 IBLA 221, 225-26 (1998)); AR479.)

the government offers a contract on a take-it-or leave it basis, it will be strictly construed against the government. *Leo Sheep Co. v. United States*, 440 U.S. 668, 680-83 (1979).

After examining a number of federal oil and gas lease agreements, this Court found that the terms of the lease contract do not impose an express duty and do not support an implied duty to market at no cost to the lessor. *IPAA v. Armstrong*, 91 F. Supp. 2d at 128; *see also United States v. General Petroleum Corp.*, 73 F. Supp. 225, 231 (S.D. Cal. 1946) (power to fix value of oil could not be implied from lease which expressly reserved to Secretary right to fix value of gas and gasoline), *aff'd sub nom. Continental Oil Co. v. United States*, 184 F.2d 802 (9th Cir. 1950) (same). The Court's ruling in *IPAA v. Armstrong* is dispositive of the issue.

D. THE USE OF AFFILIATE DOWNSTREAM RESALES IS ARBITRARY.

The next significant flaw in the 2000 rules is their disparate treatment of identical sales transactions when a lessee sells oil to an affiliate. If an independent produces 10,000 barrels of oil from a lease in a month, then sells 5,000 of those barrels to a third party at the lease for $15 per barrel, and the other 5,000 to an affiliate at the lease for $15 per barrel, the Secretary accepts $15 per barrel as the correct royalty value for the first sale, but not for the second. Instead, the Secretary demands royalties on the price received when the affiliate resells the oil downstream.[9/] New 30 C.F.R. § 206.102(a) requires the lessee to value royalty based on "the gross proceeds accruing to the

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9/ The Secretary does give the lessee in this situation the unenviable alternative of basing royalties on a downstream index price instead of the affiliate's resale price. (AR71 (30 C.F.R. § 206.103).) Either method results in excessive royalties. The Secretary will also allow some deductions from the resale price or index price for those transportation costs he deems appropriate, but none for costs he considers to be downstream "marketing" costs. (AR73 (30 C.F.R. § 206.109 (lessee may deduct "reasonable, actual costs" of transporting oil from a lease to a point off the lease).); AR72 (30 C.F.R. § 206.106 (lessee must market at no cost to the lessor)).)

(AR40M.) In that event, the non-operating lessee would owe royalties on the operator's resale price or an index price method, if the operator took its oil to an affiliate's refinery.

The Secretary's position is arbitrarily at odds with his own understanding of what a "sale" is. As is apparent from the language of the joint operating agreement (AR2457-11), the non-operating lessee gives up its title to the oil to the operator, and the operator pays consideration to the non-operator. The explicit text of the agreement makes clear that the non-operator receives value at the wellhead. (*Id.* (explaining deductions the operator may claim).) The 2000 rules define what constitutes a "sale:" the unconditional transfer of title to the oil to the buyer accompanied by the payment of consideration. (AR69R-70L (30 C.F.R. § 206.101 (defining "sale")).)[23/] The Secretary's position fails to address the text of his own regulation and must be stricken as arbitrary.

6. The Rule Arbitrarily Discriminates Against Non-Arm's-Length Exchange Transactions.

The Secretary's treatment of non-arm's-length exchange agreements under his downstream index price method is also arbitrary. If a lessee employs an arm's-length exchange agreement to "relocate" oil (in lieu of actually transporting the oil) before selling the oil outright, the 2000 rules give the lessee the option of using its downstream resale price or the downstream index price method. If a lessee employs a comparable non-arm's-length exchange agreement, the rules give the lessee no choice. It must use the downstream index price method. (AR16L; AR27M; AR37M; AR43M.) The only reason given for this restriction is that the Secretary "does not believe it is

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23/ The current definition is consistent with prior agency positions on what a "sale" is. *Arco Oil & Gas Co.*, MMS-87-0094-OCS, at 4 (1987), 8 Gower Federal Service, Royalty Valuation and Management ("The point of sale is defined as the point where title transfers and a consideration is received for the product."), *rev'd on other grounds*, 109 IBLA 34 (1989).

appropriate to use the terms of non-arm's-length exchange agreements to adjust the arm's-length gross proceeds because the differentials in such agreements may not accurately reflect market rates." (AR43M.) Once again, no reasoning is offered as to why an identical differential may be used in an arm's-length exchange agreement but not in a comparable non-arm's-length agreement.

The special irony of this arbitrary restriction is that it underscores why the Secretary's rejection of comparable sales to value oil is wrong at the core. The lessee with a non-arm's-length exchange agreement must use the downstream index price. As previously explained, however, that price must be adjusted for location and quality differentials to derive a proxy for the value of the oil at the lease. Because the lessee's exchange agreement is non-arm's-length, the lessee "must request approval from MMS for any location/quality adjustment." (AR75L (30 C.F.R. § 206.112(b)).) There are only two ways MMS can judge what an appropriate adjustment should be in this circumstance. One way would be to look to comparable arm's-length exchange agreements. If this way is chosen, then the Secretary has failed to explain why he can compare exchange agreements but not sales contracts, as IPAA had recommended he do. The second way is to compare the published index price in a given month with prices set in arm's-length sales in the field in which the lessee's lease is located. The difference between the lease price and the index price would be the differential. Of course, if this second way is chosen, it is identical to IPAA's proposed valuation procedures, for it relies on arm's-length sales at the lease, thus rendering the downstream index price superfluous.

F. THE SECRETARY'S TRANSPORTATION ALLOWANCE IS ARBITRARY.

As the Secretary sees the issue, the controversy over determining value at the lease "actually relates to downstream sales and what deductions are or are not proper in light of the lessee's duty to market." (AR58M.) As he did in the natural gas transportation rule, *see IPAA v. Armstrong*, 91 F. Supp. 2d at 126-27, the Secretary once again takes an impermissibly narrow view of what "transportation" entails.

In its comments, IPAA objected to the Secretary's refusal to base transportation allowances, when the lessee ships oil through an affiliated pipeline, on comparable arm's-length transportation contracts or on tariffs approved by FERC. (AR4105-06; AR6214-16.) Additionally, in those cases where no arm's-length contracts are available to measure an appropriate allowance for transportation, IPAA urged the Department to employ a more reasonable rate of return on invested capital, rather than limiting it to the unreasonably low "triple B bond rate." (AR2348-50.) Finally, even when a lessee ships oil at arm's length, the Secretary denies a deduction for certain costs clearly a part of transportation, so-called harboring and terminaling fees. (AR69M.)

In response, the Secretary declined to adopt any of IPAA's recommendations. The Secretary justifies his abdication of the longstanding rule that non-arm's-length transportation costs may be based on FERC tariffs on the basis that:

> [D]oing so results in allowances better reflecting lessees' actual transportation costs. There is no discrimination between producers with transportation affiliates who must use their calculated actual transportation costs and non-affiliates who may apply a FERC tariff as their arm's-length transportation cost. In both instances the parties would be deducting their actual, reasonable transportation costs.

(AR11M.) In other words, the Secretary bases his disparate treatment of arm's-length transportation and non-arm's-length transportation on the assertion that the two are not being treated differently at all. In the Secretary's view, in both cases lessees are permitted to deduct "actual, reasonable costs." This assertion fails to respond to two critical points made by IPAA.

First, the Secretary's definition of actual, reasonable costs assures that companies shipping through affiliated pipelines will ordinarily be allowed a lesser deduction than third parties shipping through the same system. Simply by denying lessees using affiliated transporters the same allowance that other lessees are permitted to take, the Secretary arbitrarily discriminates against companies choosing to invest in pipelines and other means of transportation and seeks royalty on profits earned on those transportation investments. The Department's own precedent holds that he cannot assess royalty on legitimate pipeline profits merely because a pipeline is affiliated with or even controlled by an oil producer. Such discrimination against affiliated transactions in transportation is unlawful. *See Mobil Exploration & Producing U.S. Inc.*, 148 IBLA 172, 185 (1999) (permitting Mobil to determine transportation allowance using full tariff set by pipeline, thirty-seven percent owned by Mobil, where third parties permitted to use same tariff); *Shell Western E & P Inc.*, 112 IBLA 394, 400 (1990); *Mobil Producing Texas & New Mexico, Inc.*, 115 IBLA 164 (1990). The Secretary did not and cannot explain his departure from these precedents and has failed to explain his disparate treatment of similar transportation services.

Second, the Secretary's response dodges the question of whether his definition of an "actual, reasonable" transportation allowance provides lessees a reasonable return on their investment in a pipeline. Under § 206.111 of the final rule, a lessee shipping oil not at arm's length determines its

transportation allowance based on the affiliated shipper's operating expense, maintenance expense, overhead, and a return on undepreciated capital investment equal to "the industrial bond yield index for Standard and Poor's triple B rating." (AR74R (30 C.F.R. §§ 206.111(b), (i)).) In API's opening brief, it has demonstrated thoroughly and extensively that the Secretary's use of the triple B bond rating is arbitrary, capricious and contrary to federal law, and IPAA incorporates by reference API's well-reasoned briefing on this subject. Additionally, IPAA reiterates one point it made during notice and comment regarding triple B.

When IPAA commented in April 1998, the triple B rating had been around 7.5 percent, calculated before income taxes. (AR2349.) After taxes, the effective rate was less than five percent. (*Id.*) However, no one would build an oil pipeline if the anticipated return on investment was a mere five percent after tax. (*Id.*) Put bluntly, the Secretary's limitation of the rate of return to triple B causes royalty to be assessed on pipeline profits. (*See* AR2350.) It results in the inclusion in royalty of value added by transportation. Thus, as with other policies adopted throughout these rules, the use of triple B serves to determine not value at the lease, but downstream value.

A similar, if more stark, example of Secretarial overreaching in the transportation context is defining a lessee's "gross proceeds" from production to include, "[r]eimbursements for harboring or terminaling fees." (AR69M.) Harboring and terminaling are just as much a part of transportation as is aggregation of gas, an activity which the Court determined in *IPAA v. Armstrong* to be a part of transportation because it "directly implicates the movement of multiple gas streams." 91 F. Supp. 2d at 127. Similarly, harboring and terminaling of oil are activities that occur incidentally to the

movement of oil from an offshore lease downstream to an onshore market. It is therefore unlawful to include the value added by these activities in royalty value.

G. THE RULEMAKING PROCESS WAS TAINTED BY IMPROPER INFLUENCES.

It is inevitable that disagreements will arise between the Department of the Interior and its lessees over the extent of their royalty obligations. At least one important interpretive issue has arisen every decade since federal oil and gas leasing began onshore in the 1920s, and each side has proceeded in a good faith, but vigorous dispute. Eventually, a judicial judgment -- or several in the case of take-or-pay settlements -- is needed to lay the issue to rest.

The 2000 oil rule is different in kind, however. From the beginning, some of the most influential consultants and policy advisers had undisclosed financial interests in promoting the Department's use of the downstream index price method. When these interests came to light – including the disclosure that a so-called "public watchdog" participating in the rulemaking had paid $383,600 (*see* Exhibit 4) to the Interior Department employee chiefly responsible for drafting the preamble to the January 1997 proposed rule, 62 Fed. Reg. 3742 (Jan. 24, 1997) (AR6925) -- commenters urged the Secretary to delay the issuance of a final rule until an investigation had assessed the effect these personal financial interests had on the course of the rulemaking. (AR593-04; AR09921-22; AR09931-32.[24]) Nevertheless, the Secretary refused to suspend the rulemaking pending inquiry into payments by the Project on Government Oversight ("POGO") to Interior employee Robert Berman and Department of Energy employee Robert Speir from proceeds

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[24] Interior's Office of the Inspector General and the Department of Justice's Office of Public Integrity were investigating the conduct of the federal employees. (AR09932.)

Attachment 3

Lee E. Helfrich

From: Lee E. Helfrich [helfrich@lnllaw.com]
Sent: Thursday, March 20, 2003 2:26 PM
To: Paul Knueven (E-mail)
Cc: Deborah Gibbs-Tschudy (E-mail); Lucy (E-mail)
Subject: Oil Valuation Workshops

Dear Mr. Knueven:

In the Federal Register Notice at 68 FR 7088, you are listed as the contact person for questions regarding the oil valuation workshops held earlier this month. As you may know, at the March 6 meeting in D.C., MMS officials indicated that the agency would be accepting comments until March 31, 2003. I attended the DC meeting on behalf of the California State Controller's Office and requested at that time that MMS make available certain information to facilitate the preparation of meaningful comments. I requested: (1) that MMS make its workshop notes publicly available; and (2) that MMS provide the public access to the records and analyses underlying its conclusion that its "experience" under the new oil rules suggests that amendments may be justified. With regard to (2), the MMS officials present indicated that its experience was based on material from the RIK program and one transportation allowance audit, which is apparently still in progress. Please advise whether and to what extent this material will be made publicly available prior to the close of the comment period. We would, of course, be particularly interested in independently reviewing any actual data and supporting documentation specific to California.

Thank you.

Lee Helfrich

Attachment 4

Lee E. Helfrich

From: Lee E. Helfrich [helfrich@lnllaw.com]
Sent: Saturday, August 23, 2003 11:17 AM
To: Deborah Gibbs-Tschudy (E-mail)
Cc: Lucy (E-mail); Ken Vogel (E-mail); Sharron Gebhardt (E-mail)
Subject: 68 Fed. Reg. 50087

debbie.wpd

Please see the attached request for data.

Re: Proposed Rule, 68 Fed. Reg. 50087

Dear Debbie:

I am writing to request access to information referenced in MMS's proposed rule to amend the federal oil valuation regulations. I am directing this request to you because, as you know, the principal author – Dave Hubbard – recently retired. In our recent dealings with MMS on another matter, I understand that it has been difficult to find documentation related to Mr. Hubbard's work on valuation matters, particularly studies relating to California. Fortunately, our office was able to provide MMS with copies. I assume that any difficulty associated with Mr. Hubbard's retirement does not extend to data that might support MMS's proposed changes to the oil rules. Thus, because MMS has set a short 30 day comment period for comments, I trust that MMS will be able to forward this material to us within a week.

By way of background, I note that I made a similar request for access to information during the workshop in DC last March. No data was ever received.

As I said during that workshop, it was impossible to provide comment on the specific items listed in the agenda because the agenda was not provided until the day of the workshop. The federal register notice listed only broad topics. It was also very clear that industry commenters were much more familiar with the agenda items – and, indeed, some of those items (such as the rate of return) were, as stated by Mr. Deal of the API, simply the product of an industry request that they be "run up the flagpole" again – not because of any experience under the 2000 oil rule. Both Mr. Deal and the IPAA representative conceded that there had been no industry changes since the effective date of the 2000 rule (or the 1988 rules) underlying that particular proposed change.

My firm, of course, represents the California State Controller's Office on issues of federal royalty valuation. Thus, we are most interested in obtaining the documentation evaluated or reviewed by MMS (whether generated by industry or the federal government) relating to the proposed changes for valuation of crude oil on- and off-shore California. Although there is, of course, some overlap, I have tried to narrow this request to information relevant to MMS's proposed rules as they may relate to California. Thus, this request includes:

1. All documents relating to MMS's proposal to replace ANS value with NYMEX value, including but not limited to, contracts for crude oil on- and offshore California, which reference NYMEX.

2. All documents and date reflecting MMS's "experience" (p. 50088) under the 2000 oil rules, including but not limited to, its "experience" with determining actual costs of transportation.

3. All documents and information not already contained in the administrative record of the litigation challenging the 2000 oil rules, which indicates "a potential for improving those rules in some respect" (p. 50088), including but not limited to, documents that would detail

what in the "judicial challenge to the 2000 rule led MMS to reconsider whether BBB is a sufficient rate of return" (p. 50093).

4. All documents relied upon by MMS in support of its statement (p. 50085) that there is "an issue" arising from "recent publicity and questions about information provided to spot price reporting services and the effect such potentially inaccurate information has on spot prices in general." Please also provide any data relied upon by MMS that would support its implicit position that data from these reporting services is more accurate for calculating differentials.

5. Documentation relating to the "correlation" between arm's length transactions and "public indicia of crude oil prices" referenced on p. 50089, including information on how MMS identified arm's length transactions for purposes of making the correlation.

6. All documentation examined by MMS (p. 50094) relating to the proposal for increasing the rate of return, including the API study.

7. All documentation related to the "review" of transportation allowances referenced on p. 50099.

8. All documentation related to MMS's calculation of revenue impact for California, including the underlying data used by MMS in making that calculation.

9. All documentation relating to the process for internal review of the proposed rule (e.g. surnaming).

10. All Interior records reflecting industry and/or congressional contacts regarding changes to the 2000 oil rules dated prior to February 2003.

Thanks for your cooperation.

Sincerely,

Lee Ellen Helfrich

Attachment 5

Lee E. Helfrich

From: Lee E. Helfrich [helfrich@lnllaw.com]
Sent: Tuesday, September 09, 2003 6:19 PM
To: Sharron Gebhardt (E-mail); Lucy (E-mail)
Cc: M L (E-mail); M L (E-mail); Hank Banta (E-mail)
Subject: FW:

I just sent the attached to Lucy Querques Denett. Since it relates to the proposed oil valuation rule, I'm forwarding it to you.

-----Original Message-----
From: Lee E. Helfrich [mailto:helfrich@lnllaw.com]
Sent: Tuesday, September 09, 2003 5:54 PM
To: Lucy (E-mail)
Subject: did you ever read the yaya sisterhood or did you stop at machievelli for women

lucy.wpd

-----Original Message-----
From: Katie Castonguay [mailto:katie@lnllaw.com]
Sent: Tuesday, September 09, 2003 2:50 PM
To: Lee Helfrich
Subject:

Lamberth Order.pdf

Dear Lucy:

I was sorry to learn of your recent car accident, but glad to hear that it hasn't hampered you at work. One of the only adages that I've ever trusted was "when it rains, it pours."

I understand that MRM has expressed some degree of surprise at California's opposition to the proposed rules on federal oil valuation and has indicated that it is open to working with the State.

We were of course equally surprised by MMS's proposal, particularly as it regards valuation of crude oil produced in California. However, the suggestions being made that MMS made any effort to seek input from the State on any need for amendments to those rules – technical or otherwise – is erroneous. Even at the workshop in DC, we were quite frank about our view that MMS simply does not have the experience under the 2000 rules and/or with transportation issues to support changes at this time.

If, however, MRM would like to work with the State, we would be willing to discuss California's concerns in detail. Of course, minutes of any conversation would have to be maintained and included in the public record. This should present no problem – similar minutes were maintained during the 2000 rulemaking regarding MMS's meetings with IPAA and others. It may also help to dispel any confusion regarding California's position. It might also assist us in understanding the attachment to this email.

I have been and remain only a phone call away.

Warm regards,

Lee Helfrich

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

AMERICAN PETROLEUM INSTITUTE

Plaintiff,

v.

SYLVIA V. BACA, *et al.*,

Defendants.

Civil Action No. 00-887 (RCL)

ORDER

This case comes before the Court on the Plaintiff's status report of February 26, 2003, notifying the Court that a rulemaking under consideration by the Department of the Interior may resolve some or all of the issues before the Court in this case. The Plaintiff further informs the Court that the parties will know on or about May 1, 2003, whether the rulemaking will go forward.

Upon consideration of this situation, it is hereby ORDERED that Plaintiff's motion for summary judgment [21] is DENIED without prejudice. This is not a final decision within the meaning of 28 U.S.C. § 1291.

It is further ORDERED that Defendant's motion for summary judgment [1/24/01] is DENIED without prejudice. This is not a final decision within the meaning of 28 U.S.C. § 1291.

The parties shall file a status report with the Court on or about May 1, 2003, informing the Court of the status of the rulemaking. At that time, the parties may elect to reinstate their motions for summary judgment by requesting the Court to restore them to the pending docket, or, alternatively, elect to await any further developments in the rulemaking proceeding and file periodic

26

status reports every 90 days, so long as such a proceeding is ongoing. Nothing in this Order shall preclude either party from electing to reinstate their motions for summary judgment at any time after May 1, 2003. The parties need not refile the motions.

SO ORDERED.

Royce C. Lamberth
United States District Judge

DATE: 3-14-03